TESTIMONY OF

CHARLES W. ERGEN

CEO, ECHOSTAR COMMUNICATIONS CORPORATION

BEFORE THE SENATE COMMERCE COMMITTEE

ON THE SUBJECT OF

COMPETITION TO CABLE

July 27, 1998

TESTIMONY OF
CHARLES W. ERGEN
CEO, ECHOSTAR COMMUNICATIONS CORPORATION
BEFORE THE SENATE COMMERCE COMMITTEE
ON THE SUBJECT OG
COMPETITION TO CABLE
JULY 28, 1998

Mr. Chairman and distinguished members of this Committee, thank you for providing me the opportunity to testify before you today about competition to cable. I believe DBS can be an effective competitor to cable. The technology is now here today but unfortunately some regulatory hurdles and continuing abuses of market power by cable operators are standing in the way. We urge Congress to act swiftly, remove the remaining hurdles and prevent abuse of cable power so effective competition can emerge and, at last, lower consumer bills.

My name is Charlie Ergen, and I am the founder and Chief Executive Officer of EchoStar Communications Corporation, a Direct Broadcast Satellite ("DBS") company based in Littleton, Colorado. I started EchoStar in 1980 as a manufacturer and distributor of C-band satellite dishes and grew the company by the mid-1980's into the largest supplier of C-band dishes in the world. I realized, however, that my vision of a dish in every home, school and business in the United States, and true, effective competition to cable, could not be realized with large dishes. Consequently, in 1987 EchoStar filed an application for a DBS permit with the Federal Communications Commission (the "FCC"). EchoStar has launched four DBS satellites since December 1995 and has invested approximately $2 billion in DBS, working to give consumers a choice to cable.

CURRENTLY THERE IS NO EFFECTIVE COMPETITION TO CABLE

In its Fourth Annual Report to Congress, the Federal Communications Commission reconfirmed that, despite the efforts of competitors such as DBS, cable operators continue to possess bottleneck monopoly power in the distribution of multichannel video programming.[1] Among the Commission's findings were the following:

Cable prices soared by 8.5% between July 1996 and July 1, 1997.

87% of Multichannel video subscribers receive service from their local franchised cable operator.

The number of cable subscriptions continued to grow, reaching 64.2 million.

[1] *In the Matter of Assessment of the Status of Competition in Markets for the Delivery of Video Programming*, in CS Docket No. 97-141 (rel. Jan. 13, 1998) (" Annual Report").

The proportion of television homes passed by cable grew to 97.1%.

Cable penetration in passed homes grew to 68.2%.

A trend towards regional clustering of cable television operations continued during the course of last year.

Cable industry ownership remains concentrated at the national level.

Despite marginal decline in vertical integration in terms of a percentage of cable-affiliated national satellite delivered services, cable MSOs in 1997 owned. 50% or more of 50 networks and had minority stakes in many others.

In sum, the Commission concluded: "Local markets for the delivery of video programming generally remain highly concentrated and are still characterized by some barriers to both entry and expansion by competing distributors."[2]

Recent figures suggest the trend is continuing. Earlier this month, The Commerce Department reported that cable rates have risen 7.3% while inflation overall has risen only 1.7% in the last year.[3]

The Commission also found that DBS providers in particular could not break the cable monopolies because of the lack of local programming: "[Direct to Home] satellite service, while it has certain advantages over traditional cable service, is not, by itself a direct substitute for cable service given the continued popularity of broadcast television programming and the absence of local broadcast signals from satellite distribution."[4]

Still, DBS has showed more potential to compete against cable than any other Multi-Channel Video Programming Distributor ("MVPD"). The recently announced acquisition of TCI by AT&T suggests that DBS will continue to be the leading competitor to cable. With the passage of the 1996 Act, Congress had hoped that companies like AT&T would aggressively move to build their own infrastructure directly to the home and compete against local telephone companies as well as cable operators. AT&T has chosen another route: to use the existing infrastructure of TCI rather than introduce new competition to TCI. That strategy suggests that encouraging effective competition to cable from the skies is now more important than ever before.

ECHOSTAR'S "LOCAL INTO LOCAL" PLAN

EchoStar is the only DBS company today seeking to provide consumers with a true alternative to cable. Our experience as a company (as well

[2] *Annual Report* at ¶ 11.

[3] *See* "Cable Rate Figures Could Provide Fodder For Hearing," *Communications Daily*, July 15, 1998 at 2.

[4] *Annual Report* at ¶ 11.

as
independent studies) matches the conclusions of the FCC: 8 or 10 people who walk into a satellite dealer's showroom disappoint that dealer and walk right back out because the dealer cannot show them a satellite product that gives them what they really want.[5] They can't get their local stations from satellite. Consumers spend seventy percent of their time watching their local channels when they have their TV set turned on.

In January of this year, EchoStar began offering satellite-delivered local network stations to certain consumers in the Washington, D.C., New York, Atlanta, Dallas, Boston and Chicago markets. With our fourth recently-launched satellite we will expand the offering to **Los Angeles, San Francisco, Sacramento, Portland, Seattle, Phoenix, Salt Lake City, Denver, Las Vegas, St. Louis, Chicago, Minneapolis, Miami, Pittsburgh, and San Diego** . Under current law, only customers living in "unserved households" qualify to subscribe to EchoStar's local service. Some parties have read the "unserved household" provision as excluding the majority of consumers in a local market from receiving their own local stations. EchoStar disagrees with that reading, but has for now decided to limit its service to only a small fraction of the population in the 20 cities we have targeted rather than the 40% of all U.S. residents living in those cities. In each of these markets we offer the four network stations and in some cities a couple of independents as well. While we would love to offer even more local signals, we strongly believe our plan will serve the public interest by offering for the first time many consumers in those markets a true choice between our service and cable.

We of course believe it is necessary for Congress to clarify and expand the ability of satellite carriers to offer local network signals to local markets. We therefore applaud those parts of the pending bills (S.1822 in the Senate and HR 3210 in the House), that achieve this. Unfortunately, as currently drafted, those bills come with a poison pill and would result in no consumers being offered local signals over satellite. Specifically, the must-carry provisions of the bills would not allow us to retransmit any local signal in a local market unless we also retransmit every single broadcast signal in that market.

(1) Must-Carry is Inappropriate Because of Satellite Carriers Capacity Constraints

With almost 200 broadcast stations in the 20 largest U.S. metropolitan centers, we are unable to provide each of these signals to its local market because of limited capacity. Unlike cable, which has a separate headend for each market, our satellites must use limited bandwith to serve most parts of the country. This means that satellite capacity devoted to serving New York

[5] *See Annual Report* at ¶ 58 n. 201.

subscribers cannot currently be reused to serve Philadelphia or Washington.

A detailed description of EchoStar's satellite capacity will illuminate our capacity constraints. EchoStar has decided to dedicate to local signals a substantial part of two satellites -- on the East and West Coast respectively. On EchoStar's East Coast satellite, the FCC has given us firm authority to use 11 DBS transponders; with a 6:1 digital compression ratio this means 66 video channels. Of those 66 channels, we are devoting 45 to providing 10 local markets with local programming; we will use the remaining 21 channels for niche, cultural and educational programming (EchoStar and other DBS providers are required to set aside 4-7 % or their capacity for educational programming). Our West Coast satellite will use 16 DBS transponders (or 96 video channels). With 45 channels again dedicated to providing 10 local markets in the Western half of the nation their local signals, we will be able to provide 4-6 local stations to each of those cities. These 90 channels, dedicated to local TV will complement the regular cable fare we offer with 21 DBS transponders at our "full conus" central location. These numbers are dramatically short of the 170 channels we would be required to dedicate to offer all broadcast stations in those 20 cities.

Thus, if EchoStar had to carry every station in each market we serve, we would be forced to abandon the service because the alternative -- offering all
local signals in only five markets -- is not economically practical.

There are others who agree with us. In a recent filing with the U.S. Copyright office, in support of EchoStar's ability to offer a local into local service, the staff of the Federal Trade Commission (“FTC”) -- whose mission it is to ensure competition and safeguard the American consumer -- argues that consumer welfare would be best served if DBS were exempt from "must-carry" rules.[6] If "must-carry" is applied to DBS, the filing says, "a DBS operator could be compelled to carry as many as 20 local broadcast signals from each television market. This could include affiliates of foreign language and religious networks, which typically include virtually no local content and whose network feeds are already carried by DBS operators, and channels with insignificant numbers of viewers, such as infomercial channels." The FTC filing agrees with EchoStar that this would substantially "undermine DBS' ability to deliver local channels and overcome its present competitive disadvantage."

There may come a time when a satellite provider can offer all stations in all markets. Capital Broadcasting -- a coalition of broadcasters -- has

[6] *In re Satellite Carrier Compulsory License: Definition of Unserved Households*, Reply Comments of the Staff of the Federal Trade Commission, Lib. of Cong., Copyright Office, Docket No. RM 98-1 (filed Mar. 27, 1998).

proposed such a plan and would like to make its service available to all DBS service providers. But unfortunately, that plan is four to five years away and is technologically speculative. Capital has not even begun construction of its satellite system. The system is to use very high frequencies -- the Ka-band -- which experience signal attenuation and rain fade problems. The technology for using these frequencies has yet to be commercially implemented let alone for the purpose of Direct-to-Home video. The FCC requires satellites using that spectrum to be very close to one another, necessitating larger dishes. In fact, the permissible size of the dish is still an unknown. The integration of such an offering with the current DBS services, which use different spectrum, conditional access, and digital transport standards may also be problematic.

2. Must-Carry Is Inappropriate At this Point Because Satellite Carriers Lack Market Power

Even setting aside the capacity constraints, it would be inappropriate for Congress to impose a must-carry requirement on satellite carriers at this point. The main reason why Congress imposed must-carry on cable operators, and why the courts found it constitutional, was the bottleneck characteristics of cable systems. Satellite carriers in general, and EchoStar in particular, lack that characteristic. Indeed, it was only when cable operators indisputably gained real bottleneck power in the early 1990s that Congress imposed must carry rules and the Supreme Court, after careful review, upheld them.

Specifically, in enacting the 1992 Cable Competition Act, Congress found that:[7]

Cable operators had considerable and growing market power over local video programming markets.

Cable served at least 60% of American households in 1992 and evidence indicated cable market penetration was projected to grow beyond 70%.

"Cable operators posses a local monopoly over cable households. Only one percent of communities are served by more than one cable system."

"Cable operators thus exercise control over most (if not all) of the television programming that is channeled into the subscriber's home . . . (and) can thus silence the voice of competing speakers with a flick of the switch.'"

"The structure of the cable industry would give cable operators increasing ability and incentive to drop local broadcast stations from their systems, or reposition them to a less viewed channel."

"Horizontal concentration was increasing as a small number of multiple system operators (MSOs) acquired large numbers of cable systems nationwide." In 1992,

[7] *See Turner Broadcasting System, Inc. v. FCC*, 117 S.Ct. 1174, 1190-96 (1997) ("*Turner II*").

the 10 largest MSOs served almost 54% of all cable subscribers compared to less than 42% in 1989. By 1994, the 10 largest MSOs controlled 63% of the cable systems, a figure projected to rise to 85% by 1996.

"Vertical integration in the industry was also increasing." In 1984, cable operators had equity interests in 38% of cable programming networks. In the late 1980s, 64% of new cable programmers were held in vertical ownership.

"Cable systems would have incentives to drop local broadcasters in favor of other programmers less likely to compete with them for audience and advertisers." As the Court explained, "independent local broadcasters tend to be the closest substitutes for cable programs, because their programming tends to be similar, and because both primarily target the same type of advertiser: those interested in cheaper (and more frequent) ad spots than are typically available on network affiliates."

Cable carriage greatly increases the ability of broadcast stations to compete for advertising, which substantially increases viewership.

"Cable has little interest in assisting, through carriage, a competing medium of communication."

Significant numbers of broadcasters had already been dropped and a substantial percentage of independent stations were not carried.

In parallel with clustering, cable systems were looking increasingly to advertising, especially local advertising, for revenue.

Stations dropped or denied carriage would be at "serious risk of financial difficulty."

On the basis of this evidence, the Supreme Court found that "it was more than a theoretical possibility in 1992 that cable operators would take actions adverse to local broadcasters."[8] A majority of the Court accepted that cable's bottleneck power represented a sufficient enough threat to the broadcasting system to justify an important government interest in the promulgation of must carry rules.

Cable wasn't always such a behemoth. Like DBS, cable was once a fledgling technology and Congress, recognizing this, took a series of actions to help it grow.

In fact, the history of cable television can easily be characterized as one of special favors and breaks from the Federal Government, allowing cable to compete against the monopolies of earlier eras. Back when broadcast television and telephone companies occupied the monopoly positions that the cable industry occupies today, cable regularly went to the government looking for help that would enable it to compete. As Rep. Edward Markey, ranking member of the House Commerce Subcommittee on Telecommunications, Trade and Consumer Protection, said in a recent hearing:

"What we've done . . . over the years, is we've said, to

[8] *Turner II*, 117 S.Ct. at 1192.

industries, to the cable industries, tell you what, we'll give you access to every television station for free, in the 1970's. We'll give you access to every telephone pole or electric pole in America, because we don't want you to have to build your own poles. Now, that's not perfect, but it gets you in the game.[9]"

For instance:

When cable was in its infancy, broadcasters tried to subject cable to common carrier regulation, arguing that cable's growth threatened them. The FCC, at cable's request, refused. Indeed, the FCC put a "heavy burden" on broadcasters who claimed economic injury from cable systems.

At the same time, broadcasters did not want to allow cable systems to retransmit their signals without permission. The cable industry fought against such a so-called "consent" requirement. In 1959, Congress sided with the infant cable industry, refusing to adopt a consent requirement for retransmission of local broadcast signals. Eventually, in *Fortnightly Corp. v. United Artists Television, Inc.*, the Supreme Court held that cable systems did not have to obtain consent of the copyright holder or pay royalties to retransmit copyrighted material on distant television signals. Congress left this decision unchanged until 1976. With the 1976 Act, Congress gave cable operators a broad compulsory license to retransmit broadcast signals.

•.In the 1960s and 1970s, local telephone companies refused to allow cable operators access to utility poles, utility ducts, and conduits, effectively preventing some operators from reaching their customers. Again, the cable industry looked to the government to step in, and Congress in 1979 enacted the Federal Pole Attachment Act in order to prevent telephone companies and other utilities from charging unreasonable rates for the attachment of cable television equipment to poles, ducts, conduits, and rights-of-way.

•.Not many years later, Congress, at the request of the cable industry, enacted the Federal Cable Act of 1984, allowing state and municipal governments to grant cable operators exclusive franchises. (Indeed, even after Congress finally prohibited exclusive franchises in 1992, courts have sanctioned "grandfathered" exclusive franchises.) That same 1984 Act granted cable operators the right to use easements or rights-of way dedicated for electric, gas, telephone, or other such utility transmission -- rendering unenforceable private arrangements which seek to restrict a cable system's use of such easements or rights-of-way. Indeed, the 1984 Act introduced vast deregulation of the cable industry. Congress re-regulated cable only in 1992, when its market power had become too formidable and the abuse of that power had become too blatant to ignore.

EchoStar is not asking for a break like those that cable operators secured so many times. At the same time, it is simply inappropriate to saddle EchoStar with an obligation that was imposed on cable operators only after (and because) they had amassed monopoly power.

[9] *Video Competition: Multichannel Programming: Hearings Before the House Subcomm. on Telecommunications, Trade and Consumer Protection of the Comm. on Commerce,* (Apr. 1, 1998) (Remarks of Rep. Markey).

Commissioner Michael Powell has observed, in a recent article for the Federal Communications Law Journal, that the Communications Act commands policy makers and industry to move away from "the monopoly oriented, over-regulatory origins of communications policy and toward a world in which the market, rather than bureaucracy, determines how communications resources should be utilized."[10] We believe if EchoStar is allowed by Congress to offer local signals, without having to carry them all from the very beginning, we can be a market-based solution to the rising prices of the monopoly cable companies. Ultimately, we would hope to present the kind of competition that could allow the Senate to deregulate cable completely. Certainly, consumers in the cities where we are able to offer our local service will have seen the last increase in cable prices and may even receive better service from their local company.

We therefore believe that, in order to create competition, Congress should amend the bills currently under consideration, or introduce new legislation that would create true competition to cable by allowing DBS to offer local stations without having to carry all of the stations until it has some level of market penetration. Accompanying local signal carriage should be the ability for DBS providers to get retransmission consent agreements with broadcasters under the same terms broadcasters give to cable. This is essential because we believe that, since we possess no power in the marketplace-broadcasters would have little incentive to offer us their signals on reasonable terms.

DISTANT NETWORK SIGNALS

The retransmission of distant network signals to households that cannot get a truly adequate network signal is as important to EchoStar as the question of local-into-local retransmission. In that connection, it is important to distinguish between retransmission of local and distant signals.

Retransmission of local signals does not threaten the network affiliate relationship, which the "unserved households" restriction was intended to protect. The signal being retransmitted by satellite is the local network signal, not that of another affiliate of the same network. For that reason we believe that local-into-local retransmissions are within the scope of the current copyright license, although as I have testified before legislation is still necessary.

With respect to distant signals, we acknowledge that retransmission of a distant signal where a local signal is truly available would compromise the network-affiliate relationship. We recognize the legitimate concerns of the broadcasters and we are not requesting that such retransmissions be permitted. On the other hand, the consumers' interests are paramount, and it is important to try to

[10] "Communications Policy Leadership," 50 Fed. Comm. L.J. 529, 534 (1998).

ensure that each and every consumer without an adequate network signal has access to a distant network signal by satellite. Two recent court decisions threaten to disenfranchise many such consumers. A Federal District Court in Florida interpreted the SHVA's "Grade B intensity" standard in a lawsuit brought by certain networks and network affiliated stations against PrimeTime 24, a satellite carrier unaffiliated with EchoStar. The Florida Court inappropriately used the Longley-Rice predictive model based on the mistaken belief that the FCC has sanctioned its use in this area (in fact the FCC has accepted a variant of the model in the digital TV area). This ruling threatens to leave hundreds of thousands of consumers without any network service.

At the same time, a second Federal District Court in North Carolina, facing the same question as that faced by the Florida Court, adopted a different definition of the term "Grade B intensity" based on that court's view that the FCC had sanctioned that definition.

Both the Longley-Rice methodology and the FCC's traditional Grade B contour model were developed to avoid interference between adjacent broadcasters. Both models are based on attenuated probabilities for receiving an adequate signal. The Grade B contours are set so that, at the border, only 50% of the households can receive an adequate signal 50% of the time with 50% confidence. They also do not take into account several other factors that further attenuate the signal on its way to the consumer's set. Therefore, while appropriate to the purpose of avoiding interference, they are inappropriate to ensure that consumers not receiving local signals have access to network service. In addition, the very notion that two District Courts could issue such different orders attempting to read what the FCC did or would have done suggests that the Commission should step in to commence a rulemaking on the meaning of "Grade B intensity." The SHVA explicitly gives the Commission jurisdiction and the power to do this, and EchoStar as well as the National Rural Telecommunications Cooperative have filed petitions requesting that the Commission institute a proceeding in this area.

The broadcasters argue that 97% of the country gets an acceptable signal via over the air broadcast. At the same time, they argue that if their signals are not carried on satellite, no one will be able to get them. If 97% of the people can get their signals over the air, one wonders, why do those signals all need to be carried on the satellite, or, for that matter, by cable.

In the Denver Grade B area, for example, the map I have attached shows that a $100,000 antenna, located at the EchoStar uplink center in Cheyenne, Wyoming is able to receive the Denver television station signals. Yet it doesn't.

The citizens of Vail, Colorado, also shown to be receiving the same signals, are getting theirs despite the fact that they have to overcome valleys and

14,000 foot mountain peaks.

My home in Littleton, which has the most sophisticated off air antenna equipment, even better than the average video buff, would, according to this map receive the signals from Colorado Springs and I can t.

PROGRAM ACCESS

Access to local programming is only one of two crucial elements necessary to allow DBS to be fully competitive in the market. The other is access to the popular channels controlled, produced, or otherwise heavily influenced by members of the cable monopoly. Access to all programming on fair and consistent terms is essential to creating real competition in the market for distribution of video and audio to the home.

We believe Congress and the FCC must pay close attention closing the loopholes of the Program Access laws and more vigilantly enforce the laws that do exist. Satellite companies have suffered because of repeated schemes by the cable companies to avoid or outright ignore the laws and consent decrees put in place to assure that satellite providers have minimal access to programming owned by cable operators.

For instance, Comcast, which owns several Philadelphia area professional sports teams, has canceled the traditional satellite backhaul of this programming in an apparent attempt to evade the obligation to make it available to satellite companies. Comcast, of course, also owns the Philadelphia cable franchise, and logically concludes that it would avoid subscriber losses to DBS, and perpetuate its monopoly if the Philadelphia consumer cannot get local professional sports from his satellite provider. We have filed a program access complaint with the FCC and hope that the Commission will vindicate us under the existing law prohibiting unfair practices and will also not let Comcast evade the separate anti-discrimination provision of the law. At the same time, it is important for Congress to extend the anti-discrimination provision to all programming by cable-affiliated vendors, whether that programming is backhauled by satellite or transmitted terrestrially.

In addition, we believe that cable companies continue to engage in price discrimination in violation of the program access rules: such violations are virtually costless to them because the remedies that the FCC has imposed so far are prospective "don t do it again." We believe the FCC should use its authority to award actual damages and punitive damages against repeat offenders. Consumers should also have a specific right to sue for violations, since they ultimately pay for

these violations through higher prices.

We believe in competition, not regulation, but while the cable monopoly persists, enforcement of the regulations that are in place is the only way to protect the consumer.

CONCLUSION

DBS as an industry has to be able to say to potential subscribers, as we have in one of our most recent advertising campaigns: “dump cable”; “we can give you what they can give you.” We're asking you and your colleagues in the House to let the consumer decide whether we have a product that competes. We think it will. Reform the law so that DBS can retransmit local programming with out having to bear the burden of must-carry until it becomes a more vigorous competitor to cable. Direct the FCC to enforce the Program Access laws so that the life blood of competition, programming, can be offered to consumers at a price that is comparable to cable.

If you take action, you will help the Direct Broadcast Satellite industry fulfill the promise made by Congress to the American People when Congress signed into law the Telecommunications Act of 1996. The promise was for competition. That's what consumers want and they shouldn't have to wait.